Ref: BN/TF/JD

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Dear Ms D'Souza

ERC0150 – NATIONAL ELECTRICITY AMENDMENT (CHANGES TO COST ALLOCATION METHOD) RULE 2013 CONSULTATION PAPER

Ergon Energy Corporation Limited (Ergon Energy), in its capacity as a Distribution Network Service Provider (DNSP) in Queensland, welcomes the opportunity to provide comment to the Australian Energy Market Commission on its *National Electricity Amendment (Changes to cost allocation method) Rule Consultation Paper*.

Ergon Energy does not support the proposed rule change. The proponent's reason for change appears counter to the intention of the National Electricity Rules (NER) regarding service classification. The resultant rule change would also impose more prescriptive and onerous Cost Allocation Method (CAM) requirements even for businesses which do not provide negotiated distribution services.

Currently none of Ergon Energy's distribution services are classified by the Australian Energy Regulator (AER) as Negotiated Distribution Services. All of Ergon Energy's services subject to regulation under Chapter 6 of the NER are subject to direct controls, either as;

- a Standard Control Service (which is subject to specific regulation under Part C of Chapter 6 of the NER); or
- as an Alternative Control Service, which gives the AER more discretion in respect of the controls placed on price or revenue.

Ergon Energy is aware that in order to have any service reclassified as a Negotiated Distribution Service, the AER would need to be satisfied that the service can no longer be subject to direct controls having regard to the Form of Regulation factors under the National Electricity Law. The clear intent of the framework is therefore to distinguish between:

- services that require more direct control over pricing over terms and conditions of access; and
- services for which pricing, terms and conditions can be left to negotiation between parties.

The proposed rule change distorts what is otherwise a reasonably clear distinction between classifications. That is, the placement of "controls" on the negotiated distribution service undermines the purpose of separately classifying them from other direct controls in the first place.

Notwithstanding the fact that Ergon Energy is not currently subject to the negotiated distribution services framework, we believe that a DNSP's CAM is unlikely to provide sufficient and/or relevant details in an appropriate format for dissemination by customers to enable greater insight to costs allocated to a particular service.

In accordance with clause 6.15.4 of the NER, Ergon Energy's CAM has been developed to give effect to and be consistent with the AER's Cost Allocation Guidelines[1] (CAG). The CAM is required to ensure costs are efficiently attributed or allocated to different distribution services and other regulated activities within the Ergon Energy group, thus ensuring prices paid by end customers are not inappropriately inflated or discounted. Among other things, Ergon Energy's CAM describes the causal allocators adopted and includes worked examples of how shared costs are allocated based on the ratio of direct costs by lines of business to effectively promote cost allocation principles in the NER. Of note, the CAM is a high level principles and policies document not a reporting instrument to be amended for actual numeric quantities (dollar, and or percentages).

Historically, Ergon Energy's CAM has changed every five years at the commencement of a new regulatory control period. The AER's review of Ergon Energy's CAM as part of the 2010-15 reset process included an intensive consultation between the AER and Ergon Energy, with the AER giving due regard to the complexities and intricacies in the methodologies adopted. Ergon Energy does not believe any benefit will derive from applying the distribution consultation procedures to the CAM and inviting wider public comment. Given that CAM information is fit for the purpose of the AER to adequately understand the business and give effect to national electricity objectives, this information is unlikely to be disseminated in a manner which meets the needs of the customer. As such, it is likely that information presented in a DNSP's CAM could be confusing to the wider public audience and may be taken out of context. Ergon Energy believes that DNSPs are best informed to understand the organisation's cost drivers and subsequently to identify what allocators will promote fairness when distributing costs across different services. Furthermore, cost allocation principles and processes are business specific, making comparability difficult.

Typically, the AER has approved the CAM to be 'locked in' for the duration of the regulatory control period with changes allowed in exceptional circumstances, and only with their prior approval. Paragraph 4.2 of the AER's CAG describes the process for amending an approved CAM and requirements for approved CAMs to be published (on AER and DNSP websites) are set in clause 6.15.4(h) of the NER providing visibility to interested parties.

Also of note, Regulatory Information Notice's (RIN) issued by the AER to Ergon Energy[2] have historically included (among other requirements) reporting of the allocation of shared costs. This information is to be used by the AER to verify Ergon Energy's correct application of the CAM and to inform benchmarking and comparative analysis between DNSPs. The RIN also requires an independent audit of whether the data and information has been prepared in accordance with the relevant AER approved CAM. An auditor's certification that RIN information has been prepared in accordance with the CAM provisions verifies compliance of a DNSP with the NER to have not allocated the same cost more than once.

Moreover, current processes for the preparation, approval and reporting of a DNSP's CAM are rigorous and intensively tested. Requirements for any change to impose more prescriptive requirements for a DNSP's CAM (approved and therefore published) to contain numeric quantities that change over time

[1] AER, Electricity distribution network service providers, Cost allocation guidelines, June 2008
[2] AER issued RIN's to Ergon Energy on 28 October 2011 and 28 September 2012 for the 2010-12 and 2012-15 regulatory years respectively.

would necessarily require more frequent changes to its CAM in aligning with budget processes. This would increase the regulatory burden on both DNSPs and the AER as additional time and resources are required for amendment and approval of the CAM. Prescriptive numeric quantities based on actual results would also increase the audit burden under the annual RIN reporting.

Finally, the AER has to date approved CAM changes in a timely manner, and well under the timeframe required to comply with the distribution consultation procedures (i.e. 110 business days)[3]. Applying the distribution consultation procedures is likely to result in more lengthy lead times for amendments to a CAM, further increasing the regulatory burden for both DNSPs and the AER.

Should you require additional information or wish to discuss any aspect of this submission, please do not hesitate to contact either myself on (07) 4092 9813 or Trudy Fraser on (07) 3228 2144.

Yours sincerely

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[3] Refer clause 6.16(c) and 6.16(e) of the NER.